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May 29, 1996

VIA FEDERAL EXPRESS

Mr. William F. Caton, Acting Secretary
Federal Communications Commission
Room 222
1919 M Street, NW
Washington, D.C. 20554

Re: CC Docket Number 96-98

Dear Mr. Caton:

Please find enclosed an original and 12 copies of the reply comments of the New Hampshire Public Utilities Commission, the New Mexico State Corporation Commission, the Utah Public Service Commission, the Utah Division of Public Utilities, the Vermont Public Service Board, and the Vermont Department of Public Service in the above docket.

I also enclose one additional copy, marked "STAMP COPY." Please date stamp this copy and return it to me in the enclosed postage-paid envelope.

Sincerely,

George E. Young
Associate General Counsel

Enclosure (postage-paid envelope)
cc: filing states

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BEFORE THE
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
Implementation of the Local Competition Provisions in The Telecommunications Act of 1996	)	CC Docket No. 96-98

REPLY COMMENTS OF

THE STATE OF NEW HAMPSHIRE PUBLIC UTILITIES COMMISSION
THE STATE OF NEW MEXICO STATE CORPORATION COMMISSION
THE STATE OF UTAH PUBLIC SERVICE COMMISSION AND DIVISION OF PUBLIC UTILITIES
THE STATE OF VERMONT PUBLIC SERVICE BOARD AND DEPARTMENT OF PUBLIC SERVICE

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The New Hampshire Public Utilities Commission, the New Mexico State Corporation Commission, the Utah Public Service Commission, the Utah Division of Public Utilities, the Vermont Public Service Board, and the Vermont Department of Public Service (collectively, the "Commenting States"), submit the Reply Comments. These Reply Comments focus on issues relating to the pricing of unbundled network elements under Section 252(d)(1) of the Telecommunications Act.

Many commenters urged the Commission to adopt pricing standards based upon a Total Service Long Run Incremental Cost ("TSLRIC") methodology. In some instances, these commenters specifically recognized the need to incorporate some contribution to joint and common costs in the wholesale prices, thus setting prices above TSLRIC.[1] Other commenters were less precise on the exact components of wholesale prices or the underlying TSLRIC methodology forming the basis for such rates. At the other end of the spectrum, several commenters, such as RBOC's NYNEX and US West, suggest that the Commission require that prices for unbundled elements be based upon historic, embedded costs.

The Commenting States do not support the establishment of any specific standard for the wholesale pricing of unbundled network functions. Instead, we strongly recommend that the Commission provide the states flexibility to determine what constitutes legitimate costs under Section 252(d)(1). This flexibility is essential to allow the states to manage the transition to a competitive telecommunications market. In fact, the wide range of proposals for wholesale pricing submitted to the Commission demonstrates the difficulty of establishing

[1] See, for example, Comments of Sprint Corporation.

a "one size fits all" approach to pricing and the need for balanced responses based upon particular company and state circumstances.

As competitive entry based upon the purchase of unbundled network elements begins to occur in the rural, high cost states such as those sponsoring these comments, states will need to balance competing concerns. Unbundled elements prices established too high will defeat the purpose of unbundling encouraging competitors to deploy facilities where use of unbundled functionalities would be more efficient. The Commenting States generally support forward-looking methodologies as the basis for establishing wholesale prices in a competitive environment. One of the Commenting States, Vermont, recently issued its Order in the first phase of a proceeding examining competitive issues.[2] That Order (a copy of which is attached) rejects methodologies such as the Efficient Component Pricing Rule and embedded cost approaches as inappropriate bases for establishing prices.

At the same time, unbundled prices set at TSLRIC will encourage competitors to use those functionalities as part of their offering of competitive services, but likely will lead to greater pressures on basic service rates. Quite obviously, prices for retail services, including basic service, cannot be established in isolation. The pricing of wholesale network elements ultimately will have a direct effect on the pricing of retail services. Thus, low wholesale prices will put pressure on incumbents to lower retail rates. Yet these incumbents may argue that they have a legal basis on which to seek recovery of prudently incurred historic costs, at least at the outset of the transition to competition. Should they succeed in such claims, the most likely source from which incumbents will seek to recover these costs will be low volume

[2] Investigation into Open Network Architecture, Docket No. 5713 (May 29, 1996).

rural ratepayers. Needless to say, in high cost rural states, this will further exacerbate differences in consumer costs between rural areas (and states) and urban areas, inconsistent with Section 254(b)(3) of the Act.[3]

The proper solution to this dilemma is to allow states flexibility in pricing unbundled network elements. This approach has the advantage of consistency with the plain meaning of the 1996 Act which specifies prices for network functions based upon cost, without defining cost. Quite clearly, Congress intended for states to define the appropriate costs (and costing methodologies), so long as they did not use proscribed cost of service approaches. States also have had extensive experience in balancing competing considerations and setting rates. And as our Initial Comments demonstrated, the Commenting States have actively pursued initiatives to enable the development of a competitive environment.[4]

The Commenting States seek flexibility in pricing unbundled network elements and do not support a Commission rule mandating that all services be priced at embedded costs as some Commenters have advocated. While unbundled function prices set at embedded cost will ensure the incumbent of recovery of all prudently incurred costs, such a pricing methodology may not lead to the most efficient result. States should retain the flexibility to consider any pricing standard provided they do so without reference to a rate-of-return or

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[3] As the Commenting States indicated in our Initial Comments and in our Comments in the Universal Service docket, price increases in rural states will require an increase in the size of the Universal Service Fund established under Section 254.

[4] The Vermont Order on competition noted above demonstrates the scope of state activities. That Order covers a wide range of competitive issues and reflects the careful balancing in which states must engage. As the Order indicates, both competitors and incumbents have generally supported its conclusions.

other rate-based proceeding.[5]

[5] Section 252(d)(1).

for the
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FCC NPRM Docket No. CC 96-98
May 29, 1996

for the

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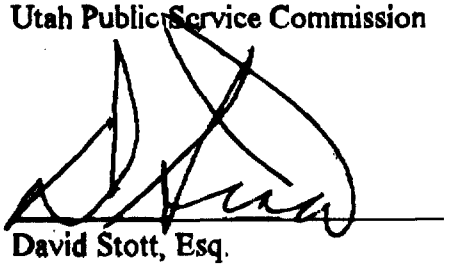

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STATE OF VERMONT
PUBLIC SERVICE BOARD

Docket No. 5713

Investigation into NET's tariff filing	)	Hearings held at
re: Open Network Architecture, including	)	Montpelier, VT
the unbundling of NET's network, expanded	)	July 21, 27-28,
interconnection, and intelligent networks	)	August 28-31, 1995
In Re: Phase I	)	

Order entered: 5/29/96

PRESENT: Frederick W. Weston, III
Hearing Officer

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PHASE I

TABLE OF CONTENTS

I. INTRODUCTION

> *This "telephone" has too many shortcomings to be seriously considered as a means of communication. The device is inherently of no value to us.*
> Western Union internal memo, 1876

This matter arose in connection with the filing by the New England Telephone & Telegraph Company ("NYNEX" or "Company") of its Open Network Architecture ("ONA") tariff on September 19, 1993. ONA describes a broad range of pricing methodologies by which a telecommunications provider (most often a local exchange company, or "LEC") makes certain elements of its network available to other competitors. In opening this investigation, the Public Service Board recognized that the issues to be explored would go well beyond the narrow set of five services offered in the tariff:

> In order to reap the benefits of competition and to promote diversity and innovation in the supply of telecommunications services (and telecommunications-based applications), competitors, enhanced service providers, and end-users must have equal and fair access to the public switched network and its manifold capabilities.
>
> The time has come, therefore, for a thorough investigation into the relevant components and functionalities of the network, their costs, and methods for pricing them and making them available to competitors, enhanced service providers, and end-users generally.[1]

It may be taken as axiomatic that today's telecommunications industry is undergoing tremendous, radical change. Rooted in rapid technological advance, the ever-expanding capabilities and shifting economics of the telephony system challenge our traditional methods—and justifications—for regulatory intervention, and warn us that even our humblest attempts to prophesy are not merely quaint (as perhaps they were in 1876), but dangerously hubristic. We may imagine the future, but hardly can we ordain it.

Even so, we are not freed of our obligations to oversee and organize certain activities so as to promote society's welfare. In the face of swiftly evolving markets, our task today is to find new ways to meet customers' growing and varied demand for services, where the efficient methods of providing those services differ wildly depending on their economic

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1. Order Opening Investigation, 2/18/94, at 6.

properties, jurisdictional assignments, and perceived benefits. More prosaically, but in practice far more complex, we must create new mechanisms that will allow for greater competitive entry in those market segments where competition promises to stimulate innovation and most efficiently meet demand for service.

More than a generation ago, the incipient technological and economic revolution in telecommunications catalyzed the regulatory processes of which this docket is a small but vital part. Competition for interstate long-distance toll traffic received early attention of policy-makers and the federal judiciary, and led eventually to the signal event of the last decade: the divestiture of AT&T's regional operating companies in 1984. Since then, the market for interstate toll service, already under pressure from alternative providers, has acceded more and more to competitive forces. Though important regulatory and technological advances were still necessary to make that competition more robust, there seems little doubt that it has generated immense benefits for the country's citizenry.

The competitive challenge spread naturally to intrastate toll. In the eleven years following the break-up of the Bell System, every state in the nation, by regulatory action or legislative fiat, authorized competitive delivery of intrastate toll service. And most recently, a number of states have set out to introduce competition into their local exchange markets, the last major component of the monopoly telephone system.

Today's report and proposed decision is a first step toward the development of a competitive local exchange market in Vermont. It recommends that the Board implement a series of new regulatory policies whose purpose is to assure the fair and orderly transition of the local exchange market from one that is essentially monopolistic in character to one that is primarily, if not wholly, competitive. This proposed decision also recommends that the Board adopt specified rules to govern critical aspects of the competitive process, most notably the terms, conditions, and pricing of competitors' access to essential monopoly facilities.

In ways that defy their foretelling, competition will fashion the composition and complexion of the nation's telecommunications industry for many years to come. The intent of today's recommendations is to harness those chaotic and creative forces to best serve our state's citizens, today and in that unknowable future.

II. BACKGROUND AND HISTORY

A. Background

On September 19, 1993, NYNEX filed its tariff for the provision of certain ONA services in Vermont. The tariff was filed pursuant to directives stemming from a comprehensive proceeding initiated by the Federal Communications Commission ("FCC" or "Commission"), the first phase of which occurred more than two years after the divestiture of American Telephone & Telegraph's Bell Operating Companies ("BOCs"). In that docket, the FCC decided to remove the structural separation between, on the one hand, AT&T's and the BOCs' common carrier operations and, on the other hand, their enhanced service and customer premise equipment operations. In its place, the FCC instituted a regime of ONA, accounting, and other non-structural safeguards to protect against cross-subsidization and anti-competitive behavior by the BOCs.[2]

On November 24, 1993, the Department of Public Service ("DPS or "Department") filed a letter and report detailing its objections to the proposed tariff and recommending that the Board suspend the tariff prior to its effective date and open "an investigation into the filing and the broader issue of Open Network Architecture and network unbundling." The Department pointed out that the proposed tariff was "new and potentially far-reaching" and raised issues that warranted a detailed investigation by the Board.[3] On February 18, 1994, the Board opened this docket.[4]

B. Statutory Authority and Essential Prior Orders

No party has raised a challenge to the Board's authority to conduct this investigation or implement rules and procedures for the competitive delivery of local exchange services.

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2. *BOC Safeguards Order*, CC Docket No. 90-623, 12/20/91, 6 FCC Rcd. 7571 (1991). *See Order Opening Investigation*, Docket 5713, 2/18/94, for more detail.

3. DPS Letter, 11/24/93, at 1, 5.

4. The Board did not, however, suspend the tariff, stating:

> Lastly, it is unclear whether, under the VTA, this tariff could be suspended as requested by the DPS. For two reasons, we decline to do so. One, the tariff creates an interim framework for dealing with ONA issues while this investigation is on-going. And two, even in its absence, we would expect NET or any other Vermont LEC to respond—in good faith and at reasonable rates, terms, and conditions—to requests for unbundled components or interconnection in the general course of business.

Order Opening Investigation, 2/18/94, at 8.

Still, a review of the applicable statutes and relevant case law offers some added context for the findings of fact and discussion that follow.

1. Title 30

Title 30 of the Vermont Statutes Annotated sets out the Public Service Board's jurisdiction.[5] In numerous decisions, the Board has interpreted its authority. With respect to telecommunications providers, the Board stated that:

> the statutory scheme is complex, but its mandate is clear. Parties are subject to the jurisdiction of the Board if they meet the two-part test of offering their service to the public, and conducting a business described in section 203.[6]

Sections 203 and 209 of Title 30 give the Board broad jurisdiction over utilities in Vermont. Section 203 provides, in pertinent part, that the Board and Department shall have jurisdiction over, among others, "a person or company offering telecommunications service to the public on a common carrier basis." In addition, the statute empowers the Board to exercise its authority "so far as may be necessary to enable [the Board] to perform the duties and exercise the powers conferred upon [it] by the law."[7]

Section 209 provides the Board with jurisdiction "to hear, determine, render judgment . . . in all matters provided for in the charter or articles of any corporation subject to supervision under this chapter . . . ."[8] The same section, furthermore, provides the Board with jurisdiction in all matters respecting . . . "[t]he manner of operating and conducting any business subject to supervision under [30 V.S.A.]," and "the price, toll, rate or rental charged by any company subject to supervision under this chapter, when unreasonable or in violation of law."[9]

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5. The Public Service Board has the power of a court of record in determining and adjudicating matters over which it has jurisdiction; it may render judgments, make orders and decrees, and enforce the same by any suitable process issuable by courts in this state. 30 V.S.A. § 9. Also, the Board, with respect to any matter within its jurisdiction, "may issue orders on its own motion and may initiate rule-making proceedings." 30 V.S.A. § 2(c).

6. *Petition of Burlington Telephone Company requesting the Board to find that the restriction of resale of wide area telephone service (WATS) in New England Telephone Company tariff P.S.B. Vt. - 20, Section 10.2.1.A, is invalid.* Docket 4946, Order of 2/21/86 at 62.

7. 30 V.S.A. § 203(5).

8. *Id.* at § 209.

9. *Id.* at (a)(3)-(4).

In addition to the general jurisdictional grants of sections 203 and 209, there are other pertinent grants of jurisdictional authority in Title 30 which authorize the Board to conduct this investigation. The Board has authority over basic exchange telecommunications service contracts found under section 226a.[10] This section requires companies providing basic exchange telecommunications services to file with the Board any basic exchange services contract.[11] Section 2701 contains explicit Board authority to require interconnection. It also provides the authority to impose charges to "support the service."[12] The Board is also empowered to approve incentive regulation plans for basic exchange telecommunications providers, to review the acquisition of control of any company subject to Board authority, and to implement universal telecommunications service.[13]

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10. 30 V.S.A. § 226.

11. This section, in addition to explicitly requiring the filing of contracts for basic services, also calls for companies to file all materials which it provided to the Department during contract negotiations. *See* §§ 226(b)(1)-(7). While this section delegates negotiations to the Department of Public Service, the final product of those negotiations—the contract itself—is to be filed with the Board. After notice and a minimum 45-day period, the Board is required to hold a hearing to approve or disapprove the contract. 30 V.S.A. § 226(c). The Board also retains jurisdiction over the contract once it has been approved. 30 V.S.A. § 226(d).

12. 30 V.S.A. § 2701(a), (b).

13. 30 V.S.A. §§ 226a, 226b, 515, 7501-7525. In 1993, the Vermont legislature enacted § 226b, which provides for "incentive regulation of basic exchange telecommunications providers." The statute allows the Board to approve "alternative forms of regulation other than the traditional methods based upon cost of service, rate base and rate of return."

The statute contains criteria which must be met before the Board can approve an alternative form of regulation. Among them are the following: consistency with the state telecommunications plan [§ 226b(c)(3)], promotion of the public interest [§ 226b(c)(4)], and protection of universal service [§ 226b(c)(5)]. Any form of alternative regulation must also "provide reasonable incentive for the creation of a modern telecommunications infrastructure" [§ 226b(c)(6)], support competition [§ 226b(c)(9)], and avoid cross-subsidization of regulated services by nonregulated services [§ 226b(c)(10)].

Alternative regulation is intended to provide incentives similar to those of competitive markets, and thus can function as a transitional mechanism to competition.

2. Prior Orders

Two Board decisions in particular are central to an understanding of how the competitive telecommunications market has developed in Vermont. The first is Docket 4946, decided in 1986; the second is Docket 5608, a 1993 decision.[14]

a. Docket 4946

Nine years ago, in Docket 4946, the Board first opened Vermont's regulated telecommunications monopolies to limited competition. It also outlined the applicable statutory authority for new market entrants. The Board also concluded that telecommunication companies in Vermont have no statutory right to an exclusive franchise.[15]

In that docket, the Board reviewed a petition by Burlington Telephone Company which claimed that the tariff of New England Telephone & Telegraph Company (*i.e.*, NYNEX, then doing business as "NET") prohibiting the resale of intrastate Wide Area Telecommunications Service ("WATS") and Message Toll Service ("MTS") services violated Title 30.[16] The investigation also reviewed a petition by ComTech Pay Services, Inc. requesting that it be allowed to resell local exchange service and intrastate MTS throughout Vermont and to allow the attachment of "customer-owned coin-operated telephones" ("COCOTS") to the intrastate public switched network. The Board declared the NET tariff at issue void, and also granted ComTech Pay Services, Inc. its petition.

In addition to deciding the particular issues raised by the parties, the Board's Order in Docket 4946 had broader policy implications for Vermont's entire telecommunications market. The Board considered two general questions. The first was whether the entry into Vermont of service providers in competition with the existing monopoly providers should be

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14. *See also Generic Investigation Into the Regulation of Cellular Telecommunications Services in the State of Vermont*, Docket 5454, Order of 1/8/92. In that Docket, the Board articulated a policy for promoting competition and for minimizing regulation where competition or the potential for competition may be sufficient to protect consumers; and *Petition of Burlington Telephone Company for a Certificate of Public Good to Operate as a Reseller of Telephone Services Within the State of Vermont*, Docket 5012, Order of 5/27/86.

15. Docket 4946, Order of 2/21/86 at 26, fn. 2. The Board stated simply that "There is no statutory right to an exclusive franchise, nor is [*sic*] there any territorial boundaries implicit in Title 30, V.S.A."

16. In particular, 30 V.S.A. § 218. *See* Docket 4946, Order of 2/21/86 at 26, fn. 1. The petition asked the Board to consider whether the NET tariff was "unjust, unreasonable, insufficient or unjustly discriminatory," in violation of the statute. *Id.* at 2.

allowed. And the second was, if competitive entry were allowed, how should the new entrants be regulated, if at all, and whether it was appropriate to continue to regulate the incumbent firms as they had been prior to such entry.[17]

The Board stated that new entrants to the Vermont market would be subject to a number of statutory requirements.[18] In 1986, there were nine certificated telephone companies in Vermont, regulated both as to price of service and return on investment.[19] Also regulated were their conditions of service, including deposits, disconnections, line extensions and service quality. The Board concluded that the statutory obligations that applied to the nine existing companies should also apply to new entrants, including the requirement that they have a certificate of public good ("CPG") before offering services in-state.[20]

The Board also addressed the question of franchise exclusivity.[21] It concluded that in Vermont telecommunications providers have no statutory right to exclusive franchises.[22] With respect to the nine Vermont telephone companies, the Board stated that "they have had by tariff but not by statute the exclusive right and, by Board policy, have had the obligation to serve."[23] The Board would revisit the issue of telecommunications franchises and its own authority eight years later in Docket 5608, an investigation into the entry into local service of the first competitive access provider in Vermont.

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17. Docket 4946, Order of 2/21/86 at 25.

18. The Board cited 30 V.S.A. §§ 203(a)(5), 209, 201(a) (definitions of "company"), 102 (CPG petition and notice), 231 (parallels 102, CPG and hearing), and 225-227 (rates, filing, and amendment). *Id.* 61-63.

19. *Id.* at 26.

20. *Id.*

21. The issue of franchise exclusivity and whether or not the Board is authorized to grant such franchises was addressed in both Dockets 4946 and 5608.

22. In 1994, when it adopted the Hearing Officer's proposal for decision in Docket 5608, the Board would reiterate this point:

> Lest there be any doubt as to my ruling on this matter, I include the following portion of the Procedural Order of 12/31/92 at 7.:
>
> > First, in Docket No. 4946, the Board concluded that there is no statutory right to an exclusive franchise, and that there are no territorial boundaries implicit in Title 30, V.S.A. Vermont telephone companies are regulated as economic monopolies because of their actual economic power, rather than because of legally-protected franchises. Order of 2/21/86 at 26.

Docket 5608, Order of 3/16/94 at 78.

23. *Id.* at 26.

b. Docket 5608

In Docket 5608, the Board further opened Vermont to competition by issuing a CPG to Hyperion Telecommunications of Vermont ("Hyperion"). The CPG authorized Hyperion, a competitive access provider ("CAP"), to offer certain telecommunications services on a limited basis.[24] Specifically, the Board authorized Hyperion to provide four types of services: "carrier to carrier,"[25] "back-haul switched access,"[26] "carrier to end-user,"[27] and "point-to-point."[28]

The Board explicitly decided to restrict Hyperion's CPG to these four services. The Board reasoned that, because the listed services do not involve local switching capability and because Hyperion was explicitly limited to the four, it was not necessary "to include a separate condition prohibiting it from offering switched services."[29]

In addition to imposing particular requirements on Hyperion, the Board also reviewed the issue of franchise exclusivity. In its discussion, the Board reiterated its holding in Docket 4946: "in effect, . . . there is no bar to competition in local exchange service and . . . such competition would be acceptable."[30] The Board did, however, add a caveat:

> because the Order [in Docket 4946] was issued before the first competitive access providers had come into existence, the Board could not have been contemplating the detailed significance of CAPs [such as Hyperion] as competitors to LECs. It follows from this that the Board's statement in Docket No. 4946 should not be viewed as pre-approval for any and all kinds of competition in the local exchange market.

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24. Docket 5608, Order of 3/16/94.

25. This is a backup service purchased by an interexchange carrier ("IXC") to ensure that, if service which the IXC provides is interrupted or in use to capacity, the IXC will be able to transport communications over the facilities of another IXC. *Id.* at 5.

26. This service allows an IXC to connect its point of presence ("POP") with a local exchange company's central office.

27. For the purpose of transporting interstate (interLATA) calls, this service connects an IXC's point of presence directly with an end-user.

28. This service connects one set of customer premises equipment with that of another customer located in Vermont, thus providing direct connection between customers without use of the public switched network.

29. Docket 5608, Order of 3/16/94 at 81.

30. *Id.* at 78.